Legislative Audit Division

State of Montana

Report to the Legislature

June 2003

Financial-Compliance Audit

For the Fiscal Year Ended June 30, 2002

Department of Administration

This report contains eight recommendations to the department. Opportunities to improve department operations include:

- **Ensuring fees are commensurate with costs.**
- **Ensuring the actuarial soundness of the State Employee Group Benefits Program.**
- **Adopting rates to fund loss reserves for state self-insurance plans under Tort Defense and Risk Management.**
- **Continuing to enhance the Treasury Unit cash reconciliation.**
- **Improving compliance with state accounting policy.**

Direct comments/inquiries to:
Legislative Audit Division
Room 160, State Capitol
PO Box 201705
Helena MT 59620-1705

03-15

Help eliminate fraud, waste, and abuse in state government. Call the Fraud Hotline at 1-800-222-4446 statewide or 444-4446 in Helena.

FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Legislative Audit Division to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2003, will be issued by March 31, 2004. The Single Audit Report for the two fiscal years ended June 30, 2001, was issued on March 26, 2002. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone (406) 444-3616

Legislative Audit Division
Room 160, State Capitol
PO Box 201705
Helena MT 59620-1705

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

June 2003

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Department of Administration for fiscal year 2001-02. This report contains eight recommendations related to cash accountability and management control, state and federal compliance, fees in Internal Service Fund not commensurate with costs, and accounting issues.

The department's written response to the audit recommendations is included on page B-3 of the audit report. We thank the director and department staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

(Signature on File)

Scott A. Seacat
Legislative Auditor

Room 160, State Capitol Building PO Box 201705 Helena, MT 59620-1705
Phone (406) 444-3122 FAX (406) 444-9784 E-Mail lad@state.mt.us

Legislative Audit Division

Financial-Compliance Audit
For the Fiscal Year Ended June 30, 2002

Department of Administration

Members of the audit staff involved in this audit were Brenda Kedish, Hollie Koehler, Angie Lang, Emlyn Neuman-Javornik, Jennifer Solem, and Jeff Tamblyn.

Table of Contents

Appointed and Administrative Officials

Department of Administration	Scott Darkenwald, Director
	Steve Bender, Deputy Director
	Cathy Muri, Administrator, Administrative Financial Services
	Thomas B. O'Connell, Administrator, Architecture and Engineering Division
	Marvin Eicholtz, Administrator, General Services Division
	Brian Wolf, Chief Information Officer, Information Technology Services Division
	Anne Goodwin, Commissioner, Banking & Financial Institutions Division
	Brett Dahl, Administrator, Risk Management and Tort Defense Division
	Gerald LaChere, Director, Montana State Lottery Division
	John McEwen, Administrator, State Personnel Division
	Greg Thornquist, Chairman, State Tax Appeal Board*
	William Hooks, Attorney, Appellate Defender's Office

*Officials of entities attached to the department for administrative purposes are listed above if the entities' financial activities are included in the department's financial schedules. The Public Employees' Retirement Administration, the Teachers' Retirement System, and the Montana State Fund issue separate annual financial statements, so officials of these entities are not listed.

Department of Administration

This report documents the results of our financial-compliance audit of the Department of Administration (department) for the fiscal year ended June 30, 2002. The previous audit report contained 12 recommendations to the department. The department implemented 6 recommendations, partially implemented 3 recommendations, and did not implement 3 recommendations.

This report contains eight recommendations addressing various functions at the department. The first three recommendations deal with department Internal Service Funds, compliance with working capital requirements, actuarial soundness and loss reserves. The following three recommendations relate to the department's treasury unit cash reconciliation function and ways in which the reconciliation could be improved. The final two recommendations relate to the department's compliance with state laws and state accounting policy.

We issued an unqualified opinion on the financial schedules contained in this report. This means the reader may rely on the presented financial information and the supporting data on the state's accounting records.

The department's written response to the audit begins on page B-3.

The listing below serves as a means of summarizing the recommendations contained in the report, the department's response thereto, and a reference to the supporting comments.

Recommendation #1

We recommend the department ensure Internal Service Fund rates are commensurate with costs as required by law. 7

Department Response: Concur. See page B-3.

Recommendation #2

We recommend the department maintain the state employee group benefit plans on an actuarially sound basis and ensure reserves are sufficient to comply with section 2-18-812, MCA. 9

Department Response: Concur. See page B-4.

Recommendation #3

We recommend the department:

A. Ensure fees charged are commensurate with costs as required by section 17-8-101, MCA.

B. Establish a self-insurance and a deductible reserve fund as allowed by section 2-9-202, MCA. 11

Department Response: Concur. See page B-5.

Recommendation #4

We recommend the department reconcile cash balances on the state's accounting records to the bank records. 13

Department Response: Concur. See page B-6.

Recommendation #5

We recommend the department ensure effective internal controls exist to enable personnel to carry out their responsibilities. 14

Department Response: Concur. See page B-6.

Recommendation #6

We recommend the department clarify the February 6, 2003, policy memo for agencies. 14

Department Response: Concur. See page B-6.

Recommendation #7

We recommend the department comply with:

A. Section 2-18-308, MCA, related to employee mileage reimbursement;

B. Section 32-5-308, MCA, requiring certain information on consumer loan annual reports; and

C. Administrative rules that set guidelines for security deposits 16

Department Response: Concur. See page B-7.

Recommendation #8

We recommend the department ensure the state's accounting records accurately reflect activity of the state by fiscal year-end as required by law.. 19

Department Response: Concur. See page B-7.

Introduction

We performed a financial-compliance audit of the Department of Administration (department) for the fiscal year ended June 30, 2002. The objectives of the audit were to:

1. Make recommendations for improvement in the department's operations including internal and management controls.

2. Test the department's compliance with applicable laws and regulations.

3. Review the implementation status of the prior audit recommendations.

4. Determine if the department's financial schedules present fairly the results of its operations for the fiscal year ended June 30, 2002.

This report contains eight recommendations to the department. Other areas of concern deemed not to have a significant effect on the successful operations of the department are not included in this report, but have been communicated to management. In accordance with section 5-13-307, MCA, we analyzed and disclosed the costs, if significant, of implementing the recommendations made in this report.

As required by section 17-8-101(6), MCA, we analyzed the rates charged and fund equity in the department's Internal Service Funds. Our findings in this area are presented beginning on page 5.

Department Organization and Functions

The department provides services to other state agencies in the areas of accounting and financial reporting, warrant writing, capitol complex maintenance, state treasury services, insurance coverage, information systems development, personnel management, purchasing, and surplus property administration.

Legislation enacted by the 2001 Legislature reorganized the Department of Commerce and resulted in several programs being transferred to the Department of Administration. Effective July 1, 2001, the Lottery, Banking & Financial Institutions, Local

Government Services, and Consumer Affairs functions were transferred to the department.

The following paragraphs describe the divisions which perform the department's primary functions.

Director's Office - responsible for the overall supervision and coordination of agency programs and administratively attached boards and agencies. The Consumer Protection Division is now a part of this division and provides assistance and follow-up related to telemarketing fraud.

Administrative Financial Services Division - maintains the Statewide Accounting, Budgeting, and Human Resources System (SABHRS), establishes state accounting policies and procedures, administers the federal Cash Management Improvement Act (CMIA), processes warrants for all state agencies, and prepares the state's Basic Financial Statements. The division also provides management support (accounting, budgeting, payroll, data processing, and personnel management) services to the department. The division is responsible for the Banking and Financial Institutions program transferred to the department from the Department of Commerce.

Architecture and Engineering - manages the remodeling and construction of state buildings. The division also formulates a long-range building plan for legislative consideration each session.

General Services - manages repair and maintenance services for state agencies in the Capitol complex and several state-owned buildings in the Helena area. Under a reorganization done during fiscal year 2002, the procurement and printing function became part of this division. Procurement and printing provides centralized purchasing, printing, and mail services to state agencies located in the Helena area.

Information Technology Services - provides central mainframe computer processing services for statewide data communications networks that access the central mainframe computer. The division designs and develops data processing applications and provides continuous maintenance support. The division also provides data processing training and support, as well as consulting services for microcomputer and office automation systems. Disaster recovery facilities for critical data processing applications are also managed by the division.

Personnel - provides state agencies with a variety of human resource management programs including training, position classification and pay, collective bargaining, and employee relations. The division publishes state rules, standards and policies relating to recruitment, selection, discipline, grievance, performance appraisal, leave, and other matters. The division administers benefits plans that include health, flexible spending accounts, a sick leave fund, employment incentive awards, and health promotion.

Risk Management and Tort Defense - provides insurance coverage for state agencies, administers the self-insurance and risk management program, and defends state agencies in tort claims lawsuits.

Montana State Lottery Division - sets policy and oversees activities and procedures of the lottery. The program director coordinates the lottery's marketing, operations, security, and administration. The lottery is administratively attached to the department. However, it is audited separately from the department.

The department director chairs the Capital Finance Advisory Council (CFAC). Created by executive order of the governor, the CFAC provides oversight of state debt management by performing analysis of prospective financing, existing debt load and trends in public finance markets. The council advises the governor and the Board of Examiners.

Introduction

Financial activity of three agencies administratively attached to the department, the Teachers' Retirement System (#02-09), the Public Employees' Retirement Administration (#02-08), and the Montana State Fund (#02-05), are presented in separately issued audit reports.

Prior Audit Recommendations

The prior audit report for the two fiscal years ended June 30, 2001, contained 12 recommendations to the department. The department implemented 6 recommendations, partially implemented 3 recommendations, and did not implement 3 recommendations. Issues related to recommendations not implemented concern the Energy Procurement and Statewide Refueling Program (page 6), Bid and Performance Security (page 15), Treasury Unit cash reconciliation (page 13), Accountability for Advances (page 18), and Internal Service Fund rates (pages 5).

Internal Service Fund Rates

The department's organizational structure includes eighteen internal service funds that are used to account for the financing of goods and services provided to other department divisions, state agencies, and governments. These funds are intended to operate similar to private business; the costs of goods or services are to be recovered from customers.

Section 17-8-101(6), MCA, states: "Fees and charges for services deposited in the internal service fund type must be based upon commensurate costs. The Legislative Auditor, during regularly scheduled audits of the state agencies, shall audit and report on the reasonableness of internal service fund type fees and charges and on the fund equity balances."

During our audit of the department we reviewed the 18 internal service funds operated by the department. The objective of our work was to determine the reasonableness of fund equity balances and whether internal service fund rates are commensurate with costs for fiscal year 2002. Of the 18 internal service funds we reviewed, we noted problems with 6. Three of the six internal service funds are part of the General Services Division. The two remaining internal service funds were the Group Benefits and the Agency Insurance internal service funds. These funds are further discussed on page 7 and page 10, respectively.

The following table displays the audit history of the Internal Service Funds. The table shows the number of times each fund has not been in compliance with section 17-8-101, MCA, for the current and three previous audit reports.

Table 1

Audit Report History of the Internal Service Funds

	1997	1999	2001	2002
ITSD Proprietary		X		
Mail & Messenger	X		X	
Intergovernmental Training	X	X		
Investment Division				
Rent & Maintenance	X	X		
Publications & Graphics				
Central Stores			X	X
Agency Insurance			X	X
Management Services				
Energy Procurement	X	X	X	
Group Benefits				X
DP Unit Proprietary				
Statewide Fueling Program	X	X	X	X
Payroll Fund				
Warrant Writing	X		X	
Human Resources				X
Procurement Card Purchase			X	X
Legal Services				

Source: Compiled by the Legislative Audit Division.

The following sections below discuss the internal service funds where rate calculations were not reasonable during this audit period.

Statewide Fueling Program

The department manages the Fueling Program internal service fund. The fund provides a fueling network for state and local government vehicles. In the prior three audit reports, and again in this report, we noted the department is not properly accounting for all financial activities. The department omits the personal services cost of the person who administers the program from the rate calculation. In order for the program to be operated on a fee commensurate with cost basis, all true costs should be included in the calculation of fees charged for services. The department has concurred with each of the three prior audit recommendations, but has taken no corrective action.

Procurement Card Purchase Internal Service Fund

In the previous audit report, and again in this report, we noted the Procurement Card Purchases Internal Service Fund fees exceeded costs. The fund received $14,467 and expended $8,133. Personnel stated whenever revenues are not commensurate with costs the department will recommend an adjustment to the legislature. Currently, revenue in this fund is derived from a $1 per card monthly fee. Fees set by the legislature are the maximum amount the department can charge. The department is allowed to reduce rates to ensure rates are commensurate with costs without legislative approval.

Central Stores Internal Service Fund

The Central Stores Internal Service Fund working capital at June 30, 2002, exceeded the 60-day maximum by $617,468. According to department management, fees were increased to help with cash flow difficulties. This issue was also noted in the previous audit report.

Human Resource Internal Service Fund

The Human Resource internal service fund did not recover the true cost of operation in fiscal year 2001-02. The fund received $116,745 and expended $143,756. Agency personnel stated they did not include compensated absences when they were determining their rate calculation. In order for fees to be commensurate with cost, the agency needs to include all true costs when calculating rates.

Recommendation #1

We recommend the department ensure Internal Service Fund rates are commensurate with costs as required by law.

Employee Group Benefit Plans Actuarial Soundness

The Department of Administration is responsible for the administration of state employee group benefits plans. The department provides state employees with health, medical, disability, life, and other related benefits. Section 2-18-812, MCA, states, "The department shall maintain state employee group benefit plans on an actuarially sound basis and maintain reserves sufficient to liquidate the unrevealed claims liability and other liabilities of state employee group benefit plans."

During the current audit, we noted fund balances in the Group Benefit Plans fund decreased from $28,544,030, at June 30, 1998, to $(2,757,918) at February 28, 2003, a $31.3 million decrease in 56 months. This decrease indicates the department has not maintained these plans on an actuarially sound basis.

According to department management, while medical and prescription costs continued to increase, the state and its employees did not see the full effect of those increases because premiums were partially subsidized by the reserves.

The excess reserves were exhausted in 2001, with the result that the group benefits plan, beginning in 2002 and continuing into 2003, has been financed on a "pay-as-you-go" basis. "Pay-as-you-go" is a method of financing under which contributions are generally made at about the same time and in about the same amount as payments and expenses come due. This method generally does not include any funding element for catastrophic events or significant increases in actual claims over projected claims.

The table below summarizes the revenue and expenditure activity, fund balance and the incurred but not reported liability (IBNR) for the past three years and the current year. The IBNR liability is an estimate of the claims that have occurred but have not yet been reported to the department. Department personnel estimate the IBNR at June 30 of each fiscal year and record the necessary transactions on the accounting records.

Table 2

Group Benefits Fund Activity

	Fiscal Year 2000	Fiscal Year 2001	Fiscal Year 2002	Fiscal Year 2003 (through February)
Fund Balance, July 1	$ 23,741,760	$ 20,757,180	$ 16,857,899	$ 6,836,218
Revenues	$ 59,882,824	$ 61,921,092	$ 66,918,253	$ 42,594,505
Expenditures	$ (62,867,404)	$ (65,820,373)	$ (76,939,934)	$ (52,188,641)
Fund Balance, June 30	$ 20,757,180	$ 16,857,899	$ 6,836,218	$ (2,757,918)
Incurred But Not Reported (IBNR) Liability	$ 7,080,097	$ 7,181,391	$ 9,163,948	——

Source: Created by the Legislative Audit Division from the Statewide Accounting, Budgeting, and Human Resource System (SABHRS) and department records.

Based on the information disclosed above, we believe rates are inadequate to maintain the state employee group benefit plan on an actuarially sound basis as required by section 2-18-812, MCA. According to department personnel, the department performed an analysis of rate adequacy as required by section 2-18-811, MCA, and concluded rates were not adequate due to unforeseen spikes in utilization and costs during October, November, and December of 2002. We reviewed 2002 billed medical claims data and determined medical claims had generally increased steadily throughout calendar year 2002; the medical claims did not suddenly increase during the last three months of the year.

Department management has indicated they are in the process of developing corrective actions to ensure the group benefits plans comply with state law.

Recommendation #2

We recommend the department maintain the state employee group benefit plans on an actuarially sound basis and ensure reserves are sufficient to comply with section 2-18-812, MCA.

Tort Defense and Risk Management

The Risk Management Division is responsible for the acquisition and administration of all insurance purchased for the protection of the state. The division provides a comprehensive insurance plan for state agencies in amounts determined and set by the Department of Administration. The plans may include property, casualty, liability, crime, fidelity and any such other polices of insurance, as the division deems reasonable and prudent. Each fiscal year the division, through an actuary, determines the amount of estimated claims liability related to potential claims under the self-insured plans. In fiscal year 2002 the estimated claims liability of $29,848,481 was recorded in the internal service fund. This liability, which is a liability that must be recorded under state accounting policy and generally accepted accounting principles (GAAP), is not considered when the division calculates its fees. By not including this liability in the rate calculation, the division is not recovering its true costs.

In accordance with section 2-9-202, MCA, the DOA may charge a sufficient amount over the actual cost of the deductible insurance to replenish the deductible reserves. In addition, the department may accumulate a reserve fund for insurance plans that is sufficient to provide self-insurance coverage. The Risk Management and Tort Defense Division currently does not have either a deductible reserve or a self-insurance reserve fund.

In fiscal year 2002, several claims were settled for an approximate total amount of $8 million, which forced the division to receive a general fund loan for the self-insurance program. If a reserve fund had been accumulated the General Fund loan may not have been necessary or the loan amount could have been reduced.

Recommendation #3

We recommend the department:

A. Ensure fees charged are commensurate with costs as required by section 17-8-101, MCA.

B. Establish a self-insurance and a deductible reserve fund as allowed by section 2-9-202, MCA.

Treasury Unit Cash Accountability and Internal Control Issues

During our audit, we noted three inter-related issues regarding the accountability and control of cash by the department's Treasury Unit. The Treasury Unit functions as the central bank for all state agencies. The following sections discuss necessary improvements to the unit's cash management system.

Unreconciled Items

- One of the Treasury Unit's primary functions is the reconciliation of cash in the state's bank account to the state's accounting records. Section 17-1-111, MCA, requires the state treasurer to receive and account for all money belonging to the state. During our audit of the Basic Financial Statements of the State of Montana (#02-01) for the fiscal year ended June 30, 2002, we found that the SABHRS cash balance on the state's accounting records was higher than the bank balance by $342,503, as of December 5, 2002. The department identified transactions contributing to the discrepancy between the bank account and accounting records and numerous corrections were made.

  As of March 20, 2003, the state's cash balances had not yet been reconciled since July 1, 1999. The accounting records reconciliation completed as of February 2003 for fiscal year-end 2002 noted the accounting system cash balance was higher than the bank by $197,892. The department is still working with agencies to identify and correct unreconciled items from fiscal years 2000, 2001, and 2002.

  As of April 3, 2003, the department had a total of 157 unreconciled items they have been working with agencies to resolve. The following table notes the status of the outstanding items in the Treasury Unit's cash reconciliation.

Table 3

Treasury Cash Reconciliation Outstanding Items

		Fiscal Year 2000	Outstanding Items	Amount
Agencies with Outstanding Items include:				
University of Montana			1	
Montana State University			5	
	Total		6	$107,756.99
		2001		
Agencies with Outstanding Items include:				
Treasury Unit			57	
Public Health and Human Services			10	
Fish, Wildlife, and Parks			10	
Department of Justice			5	
Department of Revenue			1	
Department of Transportation			1	
Department of Administration			1	
Department of Military Affairs			1	
State Fund			1	
	Total		87	$15,091.51
		2002		
Agencies with Outstanding Items include:				
Treasury Unit			41	
Public Health and Human Services			9	
Commissioner of Higher Education			3	
Public Employees' Retirement Board			3	
Department of Justice			1	
Board of Investments			1	
Department of Transportation			1	
Department of Military Affairs			1	
Department of Labor and Industry			1	
Department of Commerce			1	
State Auditor's Office			1	
Fish, Wildlife, and Parks			1	
	Total		64	$5,124.44
	Grand Total		157	$127,972.94

Source: Compiled by the Legislative Audit Division from department records.

As of April 3, 2003, the Treasury Unit had not yet received a response from the Department of Public Health and Human Services for its unreconciled items from fiscal year 2002, nor did they receive responses from the Department of Justice and the Department of Public Health and Human Services for those unreconciled items from fiscal year 2001.

Department personnel have been working to resolve the unreconciled cash balances. They developed a state policy to facilitate the cash reconciliation process. In addition, personnel developed a partially automated reconciliation tool to assist with the process. Both the cash policy and the automated reconciliation tool went into effect on March 3, 2003. Personnel indicated implementation of the cash policy and availability of an automated reconciliation tool will aid in the reconciliation process.

Recommendation #4
We recommend the department reconcile cash balances on the state's accounting records to the bank records.

Department of Transportation Cash Reconciliation

- In performing the reconciliation of cash transactions for the Department of Transportation (DOT), the treasury has experienced much difficulty tracking deposits from the state's accounting system to the deposits received for DOT. The DOT, separate from the Treasury Unit, reconciles all deposits to the state's accounting records on a monthly basis and forwards the information to the Treasury Unit. One individual within the Treasury Unit uses the DOT reconciliation to assist in one portion of the treasury cash reconciliation process. Another employee involved in the reconciliation found the information DOT furnished less useful because it did not include SABHRS document numbers. DOT has agreed to furnish the SABHRS document numbers.

Information and communication is one of the five components of an effective internal control structure. The Information and Communication component is defined as pertinent information identified, captured, and communicated in a form and timeframe that enables people to carryout their responsibilities.

Recommendation #5
We recommend the department ensure effective internal controls exist to enable personnel to carry out their responsibilities.

State Policy Memo Clarification

- The department issued a new accounting policy memo on February 6, 2003, to help facilitate a timely and effective cash reconciliation process between SABHRS and the custodial bank.

The memo exempts certain agencies from the policy. However, the department had intended the memo to apply to all agencies. This was not made clear in the final policy memo.

Recommendation #6
We recommend the department clarify the February 6, 2003, policy memo for agencies.

Noncompliance With State Laws

The Department of Administration is responsible for the implementation and monitoring of certain laws contained in the Montana Code Annotated (MCA). The department is also responsible for promulgating state accounting policy. The following sections note areas where the department was not in compliance with specific state laws and where accounting policy conflicts with state law or is unclear.

Mileage Reimbursement Rates

As part of the department's duties it sets travel policy, including reimbursement for expenses such as meals, lodging, and personal car mileage. During the August 2002 Special Legislative Session, House Bill 6 modified the reimbursement amount for mileage in section 2-18-503, MCA. Subsection (2)(a), was modified to reimburse state employees for personal car mileage when a state vehicle was available at the rate of 52 percent of the "low mileage rate" allowed by the IRS for the current year. Prior to this change, the law had allowed for reimbursement at a rate of three cents less per mile than the mileage rate allowed by the IRS for the current year.

The department, in interpreting the modified statute, assumed that the "low mileage rate" of the IRS was the standard business rate reduced by three cents. The 52 percent was then applied to the modified rate rather than directly to the standard business rate as specified by the modified law. Department personnel stated that they believed they had calculated the rate consistent with legislative intent.

Consumer Loan Annual Reports

Section 32-5-308, MCA, states the annual reports submitted by consumer loan businesses shall include a reconciliation of surplus or net earnings with the businesses' balance sheets and a schedule of assets used in the consumer loan business. We reviewed the form prescribed by the department for this reporting and noted that the forms do not request this information be submitted. Department personnel stated that this law has remained unchanged since 1959 and no longer reflects how consumer loan businesses operate.

Security Deposit Payee

During our prior audit, we noted the department did not comply with state administrative rules providing that "Certificates of Deposit or money market certificates will not be accepted as security for bid, proposal, or contract unless the certificates are assigned only to the state." During this audit, we again observed four performance security deposits were not made payable solely to the state of Montana. The securities we noted required both the signature of the contractor and the state in order for the securities to be redeemed. There is a potential loss to the state in the event that the vendor does not comply with the terms of the contract and then does not agree to sign the security for redemption by the state. Department personnel stated they were not sure why these securities did not comply with the rules.

Recommendation #7
We recommend the department comply with:

A. Section 2-18-503, MCA, related to employee mileage reimbursement;

B. Section 32-5-308, MCA, requiring certain information on consumer loan annual reports; and

C. Administrative rules that set guidelines for security deposits.

Accounting Controls

The Department of Administration uses the modified accrual basis of accounting as defined by state accounting policy for recording General Fund, Special Revenue Fund, Capital Projects Fund, and Debt Service Fund transactions. Under the modified accrual basis, revenues are recorded when the department receives cash or when receipts are measurable and available to pay current period liabilities, and expenditures are recorded for valid obligations when the department incurs the related liability and it is measurable, with the exception of the cost of employee’s annual and sick leave. In addition, the department uses the accrual basis of accounting as defined by the state accounting policy for recording Enterprise Fund, Internal Service Fund, Private-Purpose Trust Fund, Pension Trust Fund, and Agency Fund transactions. Under the accrual basis, revenues are recorded when earned and measurable and expenses are recorded in the period they are incurred when measurable. During this audit we noted several transactions that were not recorded in accordance with the state accounting policy. The following sections discuss instances where the department could improve compliance with state accounting policy.

Depreciation of Capital Assets.

The asset management (AM) module of the SABHRS computes depreciation expense for capitalized assets. The AM information is then integrated into the general ledger. If a "program year" is entered onto the AM module when the asset is added, AM then charges the depreciation beginning this program year and continues until the asset is fully depreciated. SABHRS uses the program year field to determine if the expenditure item is a current year expenditure or prior year expenditure. This causes any depreciation calculated for assets with an associated program year other than the current fiscal year to be recorded as prior year expenditure activity on SABHRS.

Section 17-2-101, MCA, states, "the financial records of the state [are to] accurately reflect the state's revenue, expenditures, expenses, and financial position in accordance with generally accepted accounting principles." According to GAAP depreciation expense should be recorded in the year in which the expense was incurred.

This difference affects only proprietary funds with capital assets. In fiscal year 2001-02, $5,883,949 was incorrectly recorded as prior fiscal year expense for the state as a whole. For the Department of Administration, the depreciation incorrectly charged as prior fiscal year expense was $1,760,269.

Prepaid Expense Classification Error

During fiscal year 2002, the department recorded the refund to the federal government for the Montana State Fund dividend as a prepaid expense. The department received a dividend from the Montana State Fund, which was recorded as a revenue to the Worker's Compensation Dividend account. The department then refunded the federal portion of the dividend, classifying this payment as prepaid expenditure. Using the prepaid expenditure classification essentially pays the charge while showing the cost as an asset, since it is deemed paid in advance of the liability. This also circumvents the budget approval requirements in the SABHRS, allowing the charge to be paid without being posted against a valid appropriation. This violates the Montana State Constitution, Section 14, Article 8, which states, "Except for interest of public debt, no money shall be paid out of the treasury unless upon an appropriation made by law…"

Department personnel indicated that all appropriation authority was used up, they were in the fiscal year end time period, and they needed to refund the Federal Department of Health and Human Services portion of the State Fund dividend immediately. A prepaid expense account was used to get the payment out.

Account Reconciliations

During our current audit, we noted the department had several balance sheet account balances that were unreconciled. The Long-Term Notes and Loans Receivable, Construction Advances, Reserve for Long-Term Advances and Fund Balance – Reserved accounts had not been reconciled from the state's general ledger to the detailed account ledger. Section 17-1-102(4), MCA, requires all state agencies input all necessary transactions to the accounting system as prescribed in subsection (2), of the same law, before the accounts are closed at the end of the fiscal year in order to present the receipt, use, and disposition of all money and property for which the agency is accountable in accordance with GAAP. The reconciliation process is a key control in ensuring all necessary transactions are input into the accounting system. Without reconciling account balances, the department cannot be sure the account balances recorded on the accounting records are correct.

Lease Capitalizations

During the current audit we noted amounts that should have been capitalized for lease payments made on capital assets were not complete. During fiscal year 2002 entries were made to capitalize the costs incurred. However, when the calculation was performed agency personnel did not consider amounts that had been recorded in fiscal year 2002 for amounts spent but not capitalized for the prior year. When the amount to be capitalized was calculated, personnel used the difference between what had been paid and what was shown as having already been capitalized. This net amount then became the amount capitalized.

During fiscal year 2002, an error was made in this calculation and approximately $1,120,812 was not capitalized at fiscal year end. Department personnel detected this error when a reconciliation of capital lease payments was requested by the department's accounting bureau during the preparation of the statewide Basic Financial Statements. Correcting entries were made in fiscal year 2003.

Recommendation #8
We recommend the department ensure the state's accounting records accurately reflect activity of the state by fiscal year-end as required by law.

Independent Auditor's Report & Agency Financial Schedules

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Schedule of Changes in Fund Balances & Property Held in Trust, Schedule of Total Revenues & Transfers-In, and Schedule of Total Expenditures & Transfers-Out of the Department of Administration for the fiscal year ended June 30, 2002. The information contained in these financial schedules is the responsibility of the department's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1, the financial schedules are presented on a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The schedules are not intended to be a complete presentation and disclosure of the department's assets, liabilities and cash flows.

In our opinion the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances & property held in trust of the Department of Administration for the fiscal year ended June 30, 2002, in conformity with the basis of accounting described in note 1.

Room 160, State Capitol Building PO Box 201705 Helena, MT 59620-1705
Phone (406) 444-3122 FAX (406) 444-9784 E-Mail lad@state.mt.us

Our audit was conducted for the purpose of forming an opinion on the basic financial schedules taken as a whole. The Schedule of Internal Service Fund Activity, on page A-13, is presented for the purposes of additional analysis and is not a required part of the financial schedules of the Department of Administration. Such information has been subjected to the auditing procedures applied in the audit of the financial schedules and, in our opinion, is fairly stated, in all material respects, in relation to the financial schedules taken as a whole.

Respectfully submitted,

(Signature on File)

James Gillett, CPA
Deputy Legislative Auditor

April 4, 2003

DEPARTMENT OF ADMINISTRATION
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Private Purpose Trust Fund	Permanent Fund	Pension Trust Fund	Unexpended Plant Fund	Renewal & Replacement Fund
FUND BALANCE: July 1, 2001	$ 196,329,090	$ 2,107,926	$ (340,107)	$ 3,489,615	$ 25,967,630	$ 1,201,713	$ (4,601,903)	$ (2,363)	$ 0	$ 224	$ 0	$ (38,057)	$ (2,050)
PROPERTY HELD IN TRUST: July 1, 2001								$ 301,356					
ADDITIONS													
Budgeted Revenues & Transfers-In	30,321,295	2,921,062	678,959		10,230,013	38,834,848	127,929,550						
NonBudgeted Revenues & Transfers-In	90,158	1,078,193	34,469	23,054,327	326,697	100,584	51,757		(44,644)				
Prior Year Revenues & Transfers-In Adjustments	(105,310)			(65,028)	(68,764)	(1,316)	(150,353)		93,631				
Direct Entries to Fund Balance	(77,058,878)	9,510,872	6,096,154		5,481,142	581,703	150,413	2,363	880,705			856,431	44,371
Additions to Property Held in Trust								143,527					
Total Additions	(46,752,735)	13,510,127	6,809,582	22,989,299	15,969,088	39,515,819	127,981,367	145,890	929,692			856,431	44,371
REDUCTIONS													
Budgeted Expenditures & Transfers-Out	25,583,922	12,323,691	7,091,125		30,286,585	31,708,162	137,905,773				47,514	895,422	64,045
NonBudgeted Expenditures & Transfers-Out	10,391,263	43,868		23,157,349	3,826,714	7,787,604	6,650,215		312,865				
Prior Year Expenditures & Transfers-Out Adjustments	11,096	46,936			(75)	(40,317)	926,439						
Reductions in Property Held in Trust								147,380					
Total Reductions	35,986,281	12,414,495	7,091,125	23,157,349	34,113,224	39,455,449	145,482,427	147,380	312,865		47,514	895,422	64,045
FUND BALANCE: June 30, 2002	$ 113,590,074	$ 3,203,558	$ (621,650)	$ 3,321,565	$ 7,823,494	$ 1,262,083	$ (22,102,963)	$ 0	$ 616,827	$ 224	$ (47,514)	$ (77,048)	$ (21,724)
PROPERTY HELD IN TRUST: June 30, 2002								$ 297,503					

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-8.

DEPARTMENT OF ADMINISTRATION
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2001

	General Fund	Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Expendable Trust Fund	Nonexpendable Fund	Unexpended Plant Fund	Renewal & Replacement Fund
FUND BALANCE: July 1, 2000	$ 194,771,998	$ 1,447,338	$ 3,266,747	$ 27,411,035	$ 1,034,763	$ (4,419,233)	$ 1,663	$ 1,677,341	$ 224	$ (533,570)	$ (87,713)
PROPERTY HELD IN TRUST: July 1, 2000							$ 289,981				
ADDITIONS											
Budgeted Revenues & Transfers-In	31,980,881	1,581,062		21,100,323	4,130,868	118,376,272					
NonBudgeted Revenues & Transfers-In	(1,306,440)	1,188,147	23,361,766	70,518	5	(146,410)		181,351			
Prior Year Revenues & Transfers-In Adjustments	125,666	154,943	28,830			(2,268,171)		426,287			
Direct Entries to Fund Balance	(1,451,546)	11,612,353		5,173,587	210,786	(303,113)	(4,026)	(944,895)		2,062,696	221,750
Additions To Property Held in Trust							85,916				
Total Additions	29,348,561	14,536,505	23,390,596	26,344,428	4,341,659	115,658,578	81,890	(337,257)		2,062,696	221,750
REDUCTIONS											
Budgeted Expenditure & Transfers-Out	23,153,017	14,964,977		23,782,215	4,194,547	122,622,489				1,567,183	136,087
NonBudgeted Expenditure & Transfers-Out	3,226,418	66,603	23,143,501	4,005,618	(34,236)	1,137,687		459,380			
Prior Year Expenditure & Transfers-Out Adjustments	1,412,034	65,148	24,227		14,398	(7,918,928)					
Reductions in Property Held in Trust							74,541				
Total Reductions	27,791,469	15,096,728	23,167,728	27,787,833	4,174,709	115,841,248	74,541	459,380		1,567,183	136,087
FUND BALANCE: June 30, 2001	$ 196,329,090	$ 887,115	$ 3,489,615	$ 25,967,630	$ 1,201,713	$ (4,601,903)	$ (2,363)	$ 880,704	$ 224	$ (38,057)	$ (2,050)
PROPERTY HELD IN TRUST: June 30, 2001							$ 301,356				

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF ADMINISTRATION
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Private Purpose Trust Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS									
Licenses and Permits		$ 73,350				$ 1,200			$ 74,550
Taxes	$ 2,724	14				2	$ 757		3,497
Charges for Services	4,841,946	1,508,928			$ 107,430	4,549,604	119,096,880		130,104,788
Investment Earnings	13,051,303	82,710	$ 2,960	$ 613,716	95,916	148,334	1,142,215	$ 296	15,137,450
Fines and Forfeits	4,617,757	77,863							4,695,620
Sale of Documents, Merchandise and Property						33,632,273	4,864,224		38,496,497
Rentals, Leases and Royalties	329								329
Miscellaneous	10,747	1,150,724	34,463		92,135	684	643,470		1,932,223
Grants, Contracts, Donations and Abandonments		35,503						48,691	84,194
Other Financing Sources	7,585,739	1,070,163		22,375,583	10,192,465		2,083,408		43,307,358
Federal	195,598		676,005						871,603
Capital Contributions						602,019			602,019
Total Revenues & Transfers-In	30,306,143	3,999,255	713,428	22,989,299	10,487,946	38,934,116	127,830,954	48,987	235,310,128
Less: Nonbudgeted Revenues & Transfers-In	90,158	1,078,193	34,469	23,054,327	326,697	100,584	51,757	(44,644)	24,691,541
Prior Year Revenues & Transfers-In Adjustments	(105,310)			(65,028)	(68,764)	(1,316)	(150,353)	93,631	(297,140)
Actual Budgeted Revenues & Transfers-In	30,321,295	2,921,062	678,959		10,230,013	38,834,848	127,929,550		210,915,727
Estimated Revenues & Transfers-In	28,119,466	5,949,420	1,430,768		45,628,767	41,039,858	130,097,144		252,265,423
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 2,201,829	$ (3,028,358)	$ (751,809)	$ 0	$ (35,398,754)	$ (2,205,010)	$ (2,167,594)	$ 0	$ (41,349,696)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS									
Licenses and Permits	$ (3,000)	$ (23,900)				$ (800)			$ (27,700)
Charges for Services	74,821	(1,609,048)			$ (217,570)	(704,428)	$ (2,814,415)		(5,270,640)
Investment Earnings	(4,581,121)	(259,507)	$ (168,046)		(360,115)	(82,563)	(169,777)		(5,621,129)
Fines and Forfeits	(143,335)	20,863							(122,472)
Sale of Documents, Merchandise and Property						(2,017,727)	184,863		(1,832,864)
Rentals, Leases and Royalties	(2,671)								(2,671)
Miscellaneous	124	379,225			(9,121)	(1,500)	253,311		622,039
Grants, Contracts, Donations and Abandonments		(376,889)							(376,889)
Other Financing Sources	6,911,414	(1,159,102)			(34,811,948)	(11)	378,424		(28,681,223)
Federal	(54,403)		(583,763)						(638,166)
Capital Contributions						602,019			602,019
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 2,201,829	$ (3,028,358)	$ (751,809)	$ 0	$ (35,398,754)	$ (2,205,010)	$ (2,167,594)	$ 0	$ (41,349,696)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-8.

DEPARTMENT OF ADMINISTRATION
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2001

	General Fund	Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Expendable Trust Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS								
Taxes	$ 349	$ 1		$ 56	$ 4	$ 957		1,367
Charges for Services	4,793,476	21,430	$ (543,755)	(68,055)	4,125,566	107,645,719		115,974,381
Investment Earnings	21,531,903	251,100	1,755,380	301,313	5,303	2,738,136	$ 4,188	26,587,323
Fines and Forfeits	4,061,346							4,061,346
Sale of Documents, Merchandise and Property						5,242,942		5,242,942
Rentals, Leases and Royalties	1,851							1,851
Miscellaneous	62	105,201		82,370		308,865		496,498
Grants, Contracts, Donations and Abandonments	1,581	222,489				5,529	603,450	833,049
Other Financing Sources	209,202	1,048,994	22,178,971	20,855,157		19,543		44,311,867
Federal	200,337	1,274,937						1,475,274
Total Revenues & Transfers-In	30,800,107	2,924,152	23,390,596	21,170,841	4,130,873	115,961,691	607,638	198,985,898
Less: Nonbudgeted Revenues & Transfers-In	(1,306,440)	1,188,147	23,361,766	70,518	5	(146,410)	181,351	23,348,937
Prior Year Revenues & Transfers-In Adjustments	125,666	154,943	28,830	0	0	(2,268,171)	426,287	(1,532,445)
Actual Budgeted Revenues & Transfers-In	31,980,881	1,581,062	0	21,100,323	4,130,868	118,376,272	0	177,169,406
Estimated Revenues & Transfers-In	31,626,398	3,506,997	0	69,871,204	4,857,419	151,077,315	0	260,939,333
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 354,483	$ (1,925,935)	$ 0	$ (48,770,881)	$ (726,551)	$ (32,701,043)	$ 0	$ (83,769,927)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS								
Licenses and Permits	$ (3,000)							$ (3,000)
Charges for Services	53,641	$ 19,730		$ (243,055)	$ (725,853)	$ (33,851,999)		(34,747,536)
Investment Earnings	2,087,272	(97,862)		(15,048)	(698)	526,124		2,499,788
Fines and Forfeits	(340,312)							(340,312)
Sale of Documents, Merchandise and Property						1,168,676		1,168,676
Rentals, Leases and Royalties	(1,149)							(1,149)
Miscellaneous	(38)	(751,635)		(30)		207,791		(543,912)
Grants, Contracts, Donations and Abandonments		(254,997)						(254,997)
Other Financing Sources	(1,392,268)	(1,039,165)		(48,512,748)		(751,635)		(51,695,816)
Federal	(49,663)	197,994	$				$	148,331
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 354,483	$ (1,925,935)	$ 0	$ (48,770,881)	$ (726,551)	$ (32,701,043)	$ 0	$ (83,769,927)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF ADMINISTRATION
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

PROGRAM (SUBCLASS) EXPENDITURES & TRANSFERS-OUT	ADMIN FINANCIAL SERV DIVISION	APPELLATE DEFENDER	ARCHITECTURE & ENGINEERING PROGRAM	BANKING & FINANCIAL DIVISION	CORRECTIONS	DEPARTMENTS & AGENCIES	DPHHS	GENERAL SERVICES PROGRAM	INFORMATION TECH SERV DIVISION	MAIL & DISTRIBUTION BUREAU	MONTANA STATE LOTTERY	RISK MANAGEMENT & TORT DEFENSE	STATE PERSONNEL DIVISION	STATE TAX APPEAL BOARD	UNIVERSITY SYSTEM	Total
Personal Services																
Salaries	$ 1,712,857	$ 107,024	$ 643,270	$ 850,283				$ 2,425,245	$ 7,649,766		$ 962,667	$ 519,292	$ 1,456,284	$ 147,045		$ 16,473,733
Other Compensation				150							27,289			1,845		29,284
Employee Benefits	446,421	26,888	152,469	211,633				706,069	1,818,418		267,831	131,362	383,712	36,444		4,181,247
Personal Services-Other	45,269							(5,405)	86,685		(4,462)	8,081	(4,493)			125,675
Total	2,204,547	133,912	795,739	1,062,066				3,125,909	9,554,869		1,253,325	658,735	1,835,503	185,334		20,809,939
Operating Expenses																
Other Services	456,113	12,461	124,876	46,151				2,403,040	2,923,619		5,151,514	3,827,654	2,603,399	16,979		17,565,806
Supplies & Materials	97,961	3,748	29,293	43,409				240,322	974,115		246,083	34,652	96,614	16,996		1,783,193
Communications	456,294	8,819	20,249	22,124				2,782,420	5,791,800		665,320	19,012	94,356	3,405		9,863,799
Travel	48,788	3,852	41,123	161,761				28,500	204,789		28,417	22,315	62,799	2,511		604,855
Rent	113,581	10,480	30,053	52,955				622,784	5,134,685		88,272	45,862	90,342	10,968		6,199,982
Utilities				3,386				1,637,998			11,503	5,233				1,658,120
Repair & Maintenance	9,653	77	2,819	2,714				853,927	1,933,209		22,226	569	4,849	1,577		2,831,620
Other Expenses	1,902,151	6,772	48,190	132,616				1,112,298	3,136,228	$ 10,432	18,553,461	27,244	360,181	9,012		25,298,585
Goods Purchased For Resale								8,188,094			425,515					8,613,609
Total	3,084,541	46,209	296,603	465,116				17,869,383	20,098,445	10,432	25,192,311	3,982,541	3,312,540	61,448		74,419,569
Equipment & Intangible Assets																
Equipment								5,546	18,821							24,367
Total								5,546	18,821							24,367
Capital Outlay																
Land & Interest In Land							$ (1,500)									(1,500)
Buildings					$ 10,426,956	$ 9,883,148	802,070	11,500							$ 10,772,733	31,896,407
Other Improvements								(5,546)	74,725							69,179
Total					10,426,956	9,883,148	800,570	5,954	74,725						10,772,733	31,964,086
Local Assistance																
From State Sources	1,610,011													554		1,610,565
From Federal Sources	254,152															254,152
From Other Income Sources									4,386,290							4,386,290
Total	1,864,163								4,386,290					554		6,251,007
Grants																
From State Sources	6,330															6,330
Total	6,330															6,330
Benefits & Claims																
From State Sources													75,445,260			75,445,260
Insurance Payments												12,933,539	1,982,557			14,916,096
Total												12,933,539	77,427,817			90,361,356
Transfers																
Accounting Entity Transfers	29,406,999		1,070,164		4,495,910	6,028,434	777,922	933,055			7,474,213	1,586,393				51,773,090
Total	29,406,999		1,070,164		4,495,910	6,028,434	777,922	933,055			7,474,213	1,586,393				51,773,090
Debt Service																
Bonds	23,121,825					1,793										23,123,618
Leases									118,001							118,001
Installment Purchases								34,989			133,844					168,833
Total	23,121,825					1,793		34,989	118,001		133,844					23,410,452
Total Expenditures & Transfers-Out	$ 59,688,405	$ 180,121	$ 2,162,506	$ 1,527,182	$ 14,922,866	$ 15,913,375	$ 1,578,492	$ 21,974,836	$ 34,251,151	$ 10,432	$ 34,053,693	$ 19,161,208	$ 82,575,860	$ 247,336	$ 10,772,733	$ 299,020,196
EXPENDITURES & TRANSFERS-OUT BY FUND																
General Fund	$ 33,507,854				$ 29,154	$ 1,793		$ 925,557	$ 131,050				$ 1,143,537	$ 247,336		$ 35,986,281
State Special Revenue Fund	69,691	$ 180,121	$ 1,092,342	$ 1,527,182		2,672,793	$ 1,230,801	31,118	4,423,338			$ 1,150,353	36,756			12,414,495
Federal Special Revenue Fund	306,257				4,466,756	1,854,768			463,344							7,091,125
Debt Service Fund	23,157,349															23,157,349
Capital Projects Fund	506,346		1,070,164		10,426,956	10,941,021	347,691	933,055	74,725						$ 9,813,266	34,113,224
Enterprise Fund	266,749					25,000		1,372,036			$ 34,053,693		3,737,971			39,455,449
Internal Service Fund	1,561,294					418,000		18,713,070	29,158,694	$ 10,432		18,010,855	77,610,082			145,482,427
Private Purpose Trust Fund	312,865															312,865
Pension Trust Fund													47,514			47,514
Unexpended Plant Fund															895,422	895,422
Renewal & Replacement Fund															64,045	64,045
Total Expenditures & Transfers-Out	59,688,405	180,121	2,162,506	1,527,182	14,922,866	15,913,375	1,578,492	21,974,836	34,251,151	10,432	34,053,693	19,161,208	82,575,860	247,336	10,772,733	299,020,196
Less: Nonbudgeted Expenditures & Transfers-Out	34,149,045		1,070,164			2,748,374		511,955	(199,286)		6,846,070	5,059,073	1,984,484			52,169,879
Prior Year Expenditures & Transfers-Out Adjustments	23,361	(788)	51	(3,466)				101,766	754,850	10,432	(44,265)	88,439	15,599	(1,824)	(75)	944,080
Actual Budgeted Expenditures & Transfers-Out	25,515,999	180,909	1,092,291	1,530,648	14,922,866	13,165,001	1,578,492	21,361,115	33,695,587		27,251,888	14,013,696	80,575,777	249,160	10,772,808	245,906,237
Budget Authority	26,714,243	183,112	1,172,639	2,166,069	33,827,819	82,666,670	4,502,711	22,462,325	41,875,517		29,960,621	14,916,876	81,694,131	312,005	107,368,785	449,823,523
Unspent Budget Authority	$ 1,198,244	$ 2,203	$ 80,348	$ 635,421	$ 18,904,953	$ 69,501,669	$ 2,924,219	$ 1,101,210	$ 8,179,930	$ 0	$ 2,708,733	$ 903,180	$ 1,118,354	$ 62,845	$ 96,595,977	$ 203,917,286
UNSPENT BUDGET AUTHORITY BY FUND																
General Fund	$ 773,876					$ 83,207		$ 4,659	$ 5,144				$ 30,644	$ 62,845		$ 960,375
State Special Revenue Fund	74,686	$ 2,203	$ 80,348	$ 635,421		11,349,191	$ 708,229		300,315			$ 20,825	47		$ 33,744	13,205,009
Federal Special Revenue Fund	26,908				$ 6,148,026	21,992,983	159,436		336,656							28,664,009
Capital Projects Fund	1				12,756,927	36,057,089	2,056,554		1,817,561						20,387,416	73,075,548
Enterprise Fund	104,555							109,495			$ 2,708,733		618,392			3,541,175
Internal Service Fund	218,218							987,056	2,660,799			882,355	466,010			5,214,438
Pension Trust Fund													3,261			3,261
Unexpended Plant Fund									3,059,455						75,154,929	78,214,384
Renewal & Replacement Fund						19,199									1,019,888	1,039,087
Unspent Budget Authority	$ 1,198,244	$ 2,203	$ 80,348	$ 635,421	$ 18,904,953	$ 69,501,669	$ 2,924,219	$ 1,101,210	$ 8,179,930	$ 0	$ 2,708,733	$ 903,180	$ 1,118,354	$ 62,845	$ 96,595,977	$ 203,917,286

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-8.

DEPARTMENT OF ADMINISTRATION
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2001

	PROGRAM (SUB-CLASS) NOT SPECIFIED SEE NOTE 3	ACCOUNTING & MGMT SUPPORT	APPELLATE DEFENDER	ARCH & ENGINEERING	CORRECTIONS	DEPARTMENTS & AGENCIES	GENERAL SERVICES PROGRAM	GOVERNOR ELECT PROGRAM	INFORMATION SERVICES DIVISION	MAIL & DISTRIBUTION BUREAU	PROCUREMENT & PRINTING DIV.	PUBLIC HEALTH	RISK MANAGEMENT & TORT DEFENSE	STATE PERSONNEL DIVISION	STATE TAX APPEAL BOARD	UNIVERSITY SYSTEM	Total
PROGRAM EXPENDITURES & TRANSFERS-OUT BY OBJECT																	
PERSONAL SERVICES																	
Salaries		$ 1,061,808	$ 124,206	$ 627,807			$ 731,286	$ 18,127	$ 7,278,075	$ 358,795	$ 1,365,545		$ 464,270	$ 1,316,101	$ 149,051		$ 13,495,071
Other Compensation		659													4,725		5,384
Employee Benefits		266,043	30,390	146,667			192,868	1,523	1,672,067	95,487	397,319		116,311	339,878	35,722		3,294,275
Personal Services-Other		1,893					8,788		888	539	17,953		19,122	10,079			59,262
Total		1,330,403	154,596	774,474			932,942	19,650	8,951,030	454,821	1,780,817		599,703	1,666,058	189,498		16,853,992
Operating Expenses																	
Other Services		507,711	11,676	106,094			2,088,245	19,460	3,166,153	49,779	242,956		3,218,080	2,016,728	33,913		11,460,795
Supplies & Materials		36,136	2,598	9,805			139,863	2,845	1,429,708	42,761	111,213		37,017	62,280	2,243		1,876,469
Communications		438,692	7,917	21,111			14,684	2,118	6,319,647	2,506,321	77,140		19,735	83,303	4,208		9,494,876
Travel		31,371	7,501	35,641			1,398	3,849	195,138	3,357	33,799		25,005	31,758	13,165		381,982
Rent		52,795	9,557	33,810			389,823	360	4,676,130	56,400	194,869		49,232	99,894	13,723		5,576,593
Utilities							1,689,190				22,572		4,823				1,716,585
Repair & Maintenance		4,638		2,698			742,468		1,341,371	71,218	169,643		89,403	4,850	1,333		2,427,622
Other Expenses	$ 1,261,156	1,397,027	5,978	36,969			59,217	350	(6,872,960)	15,581	267,342		31,128	299,835	12,843		(3,485,534)
Goods Purchased for Resale											8,546,740						8,546,740
Total	1,261,156	2,468,370	45,227	246,128			5,124,888	28,982	10,255,187	2,745,417	9,666,274		3,474,423	2,598,648	81,428		37,996,128
Equipment & Intangible Assets																	
Equipment	253,003	1,952		5,751					565,632	15,074	(101,311)						740,101
Intangible Assets		57,950															57,950
Total	253,003	59,902		5,751					565,632	15,074	(101,311)						798,051
CAPITAL OUTLAY																	
Land & Interest in Land						$ 360,000											360,000
Buildings	11,500				$ 813,843	10,001,105	34,500					$ 4,549,253				$ 10,225,006	25,635,207
Other Improvements											(14,400)						(14,400)
Total	11,500				813,843	10,361,105	34,500				(14,400)	4,549,253				10,225,006	25,980,807
LOCAL ASSISTANCE																	
From State Sources		1,510,649													1,318		1,511,967
From Federal Sources		248,808															248,808
From Other Income Sources									5,123,471								5,123,471
Total		1,759,457							5,123,471						1,318		6,884,246
GRANTS																	
From State Sources		17,000															17,000
Total		17,000															17,000
BENEFITS & CLAIMS																	
From State Sources														66,885,283			66,885,283
Insurance Payments													3,171,307	101,294			3,272,601
Total													3,171,307	66,986,577			70,157,884
TRANSFERS																	
Accounting Entity Transfers	30,290	21,706,047		1,048,994	295,711	6,423,601						2,911,526	320,952			95,000	32,832,121
Total	30,290	21,706,047		1,048,994	295,711	6,423,601						2,911,526	320,952			95,000	32,832,121
Debt Service																	
Bonds		23,079,061				91,887											23,170,948
Leases									1,295,841								1,295,841
Installment Purchases							29,379			2,423	3,545						35,347
Total		23,079,061				91,887	29,379		1,295,841	2,423	3,545						24,502,136
Total Program Expenditures & Transfers-Out	$ 1,555,949	$ 50,420,240	$ 199,823	$ 2,075,347	$ 1,109,554	$ 16,876,593	$ 6,121,709	$ 48,632	$ 26,191,161	$ 3,217,735	$ 11,334,925	$ 7,460,779	$ 7,566,385	$ 71,251,283	$ 272,244	$ 10,320,006	$ 216,022,365
PROGRAM EXPENDITURES & TRANSFERS-OUT BY FUND																	
General Fund		$ 24,723,246			$ 9,600	$ 91,887	$ 353,329	$ 48,632	$ 672,425		$ 494,539	$ 45,585		$ 1,079,982	$ 272,244		$ 27,791,469
Special Revenue Fund	$ 11,500	366,985	$ 199,823	$ 1,026,353	427,596	4,338,220	35,775		5,873,471			2,766,367	$ 19,543	31,095			15,096,728
Debt Service Fund		23,167,728															23,167,728
Capital Projects Fund		694,037		1,048,994	672,358	12,106,454						4,649,254				$ 8,616,736	27,787,833
Enterprise Fund	18,776										424,274	(427)		3,732,086			4,174,709
Internal Service Fund	1,525,673	1,008,864				340,032	5,732,605		19,645,265	$ 3,217,735	10,416,112		7,546,842	66,408,120			115,841,248
Expendable Trust Fund		459,380															459,380
Unexpended Plant Fund																1,567,183	1,567,183
Renewal & Replacement Fund																136,087	136,087
Total Program Expenditures & Transfers-Out	1,555,949	50,420,240	199,823	2,075,347	1,109,554	16,876,593	6,121,709	48,632	26,191,161	3,217,735	11,334,925	7,460,779	7,566,385	71,251,283	272,244	10,320,006	216,022,365
Less: Nonbudgeted Expenditures & Transfers-Out	1,526,253	26,848,192		1,048,995		2,956,623	45,234		(603,543)	(81,953)	(56,521)		207,991	113,701			32,004,972
Prior Year Expenditures & Transfers-Out Adjustments	29,696	1,419,443	(142)	(492)			17,503		(7,928,407)	(440)	32,019		(5,050)	23,367	9,378		(6,403,123)
Actual Budgeted Expenditures & Transfers-Out		22,152,605	199,965	1,026,844	1,109,554	13,919,970	6,058,970	48,632	34,723,111	3,300,128	11,359,427	7,460,779	7,363,444	71,114,215	262,866	10,320,006	190,420,516
Budget Authority		24,640,916	201,046	1,061,965	4,727,486	112,140,692	6,187,885	50,000	39,801,941	3,476,764	12,886,410	41,294,378	9,776,271	71,798,054	406,249	122,062,178	450,512,235
Unspent Budget Authority	$ 0	$ 2,488,311	$ 1,081	$ 35,121	$ 3,617,932	$ 98,220,722	$ 128,915	$ 1,368	$ 5,078,830	$ 176,636	$ 1,526,983	$ 33,833,599	$ 2,412,827	$ 683,839	$ 143,383	$ 111,742,172	$ 260,091,719
UNSPENT BUDGET AUTHORITY BY FUND																	
General Fund		$ 2,333,024	$ 869			$ 38,686	$ 3,021	$ 1,368	$ 18,489		$ 20,463	$ 29,154		$ 115,171	$ 143,383		$ 2,703,628
Special Revenue Fund		32,165	212	$ 35,121	$ 1,823,123	$ 45,274,703			139,243			10,614,782	$ 783,313	33		$ 33,744	58,736,439
Capital Projects Fund		8,120			1,794,809	52,888,134						23,186,050				32,093,341	109,970,454
Enterprise Fund											93,796	3,613		219,658			317,067
Internal Service Fund		115,002					125,894		4,921,098	$ 176,636	1,412,724		1,629,514	348,977			8,729,845
Unexpended Plant Fund																78,935,137	78,935,137
Renewal & Replacement Fund						19,199										679,950	699,149
Unspent Budget Authority	$ 0	$ 2,488,311	$ 1,081	$ 35,121	$ 3,617,932	$ 98,220,722	$ 128,915	$ 1,368	$ 5,078,830	$ 176,636	$ 1,526,983	$ 33,833,599	$ 2,412,827	$ 683,839	$ 143,383	$ 111,742,172	$ 260,091,719

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

1. Summary of Significant Accounting Policies

Basis of Accounting

The department uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental fund category (General, Special Revenue, Capital Projects, and Debt Service) and certain liabilities of defined benefit pension plans and certain post employment healthcare plans. In applying the modified accrual basis, the department records:

> Revenues when it receives cash or when receipts are measurable and available to pay current period liabilities.
>
> Expenditures for valid obligations when the department incurs the related liability and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the department to record the cost of employees' annual leave and sick leave when used or paid.

The department uses accrual basis accounting for its Proprietary (Enterprise and Internal Service) and Fiduciary (Private-Purpose Trust, Pension, and Agency) fund categories. Under the accrual basis, as defined by state accounting policy, the department records revenues in the accounting period earned when measurable and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the department receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Notes to the Financial Schedules

Basis of Presentation

The financial schedule format is in accordance with the policy of the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

Department accounts are organized in funds according to state law applicable at the time transactions were recorded. The department uses the following funds:

Governmental Fund Category

General Fund - to account for all financial resources except those required to be accounted for in another fund.

State Special Revenue Fund - to account for proceeds of specific revenue sources (other than private purpose trusts or major capital projects) that are legally restricted to expenditures for specific purposes. In fiscal year 2001 certain activity was reported in an Expendable Trust Fund, but because of the implementation of GASB 34 is now reported as part of the Special Revenue Fund. Department Special Revenue Funds include the 911 telecommunications program, Public Safety Radio, and Financial Institutions division.

Federal Special Revenue Fund - to account for funds received from federal assistance programs. Department Federal Special Revenue Funds include federal surplus property, GIS federal funding, and the federal portion of the State Fund dividend.

Debt Service Fund - to account for accumulated resources for the payment of general long-term debt principal and interest. The department uses this fund for the Long-Range Building program and information technology bond debt service.

Capital Projects Fund - to account for financial resources used for the acquisition or construction of major capital facilities, other than those financed by proprietary funds or trust funds. The department uses this fund to account for activity in the Long-Range Building program.

Permanent Fund - to account for financial resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the department's programs. In fiscal year 2001 this activity was reported under the Nonexpendable Trust Fund. The department uses this fund for School Bond Contingency Loans.

Proprietary Fund Category

Internal Service Fund - to account for the financing of goods or services provided by one department or agency to other departments or agencies of state government or to other governmental entities on a cost-reimbursement basis. Department Internal Service Funds include State Personnel, Information Services, Procurement & Printing, General Services, and Mail & Distribution funds.

Enterprise Fund - to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; or (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. Department Enterprise Funds include flexible spending funds, and surplus property.

Fiduciary Fund Category

Pension Trust Fund - to account for resources required to be held in trust for the members and beneficiaries of defined benefit pension plans, defined contribution plans, other post employment benefit plans, or other employee benefit plans. Department pension trust funds include voluntary employee benefit association trust.

Private-purpose Trust Fund - to account for activity of all (other) trust arrangements under which principal and income benefit individuals, private organizations, or other governments. This fund did not exist in fiscal year 2001 under the previous fund structure. Department private-purpose trust funds include stale dated warrants.

Agency Fund - to account for resources held by the state in a custodial capacity. The department agency funds include central payroll, bad debt collections, and the general warrant clearing account.

2. General Fund Balance

Each agency has authority to pay obligations from the statewide General Fund within its appropriation limits. The department's total assets placed in the fund exceed outstanding liabilities, resulting in positive ending General Fund balance for the fiscal year ended June 30, 2002. These balances reflect activity at the agency and not the fund balance of the statewide General Fund.

3. Expenditure Program (Subclass)

As part of the implementation of a new accounting system in fiscal year 1999-00, state officials determined that a subclass designation would identify the program to which expenditures should be charged. State officials did not require non-budgeted expenditure transactions to be identified to a subclass. The program designations in the Schedule of Total Expenditures & Transfers-Out are based on the subclass designation used when the expenditures were recorded. The accounting system did not require agencies to code non-budgeted accounts with a subclass code identifying the expenditure program in which the activity occurred until September 2000. This new edit requires that all expenditure transactions entered through the general ledger include a subclass value.

4. Direct Entries to Fund Balance

Direct entries to fund balances in the General, Special Revenue, Capital Projects, Internal Service, Enterprise, Agency and Private Purpose funds include entries generated by SABHRS to reflect the flow of resources within individual funds shared by separate agencies. The department is the administrator of the statewide General Fund. The direct entry to fund balance in the amount of $77 million reflects the department closing out cash entries. Within the other funds, there are shared accounts with other state agencies. One agency may record revenue and another agency will record expenditure. Direct entries to fund balance occur to consolidate cash balances at fiscal year end.

5. Accounting Entity Transfers

In the Administration and Financial Services Division shown on the Schedule of Total Expenditures & Transfers-Out, there is a $29,406,999 transfer. The majority of this dollar amount is to remove bond activity from the Department of Administration's records and disburse to individual agencies records as required by GASB 34.

6. Subsequent Events

In July 2002, the department issued $10.475 million in General Obligation Long Range Building Program Bonds, series 2002B.

In October 2002, the State of Montana issued $15.805 million of General Obligation Refunding Bonds, series 2002D.

In October 2002, the State of Montana issued $92.8 million in Tax and Revenue Anticipation Notes.

Department Response

DEPARTMENT OF ADMINISTRATION
DIRECTOR'S OFFICE

JUDY MARTZ, GOVERNOR
MITCHELL BUILDING
STATE OF MONTANA
(406) 444-2032
FAX 444-2812
PO BOX 200101
HELENA, MONTANA 59620-0101

June 2, 2003

Scott Seacat
Legislative Auditor
Legislative Audit Division
State Capitol
Helena, MT 59620

Dear Mr. Seacat:

We have reviewed the recommendations pertaining to the Financial-Compliance Audit for the fiscal year ended June 30, 2002. Our responses are as follows:

RECOMMENDATION #1: WE RECOMMEND THE DEPARTMENT ENSURE INTERNAL SERVICE FUND RATES ARE COMMENSURATE WITH COSTS AS REQUIRED BY LAW.

Response: We concur.

Human Resource Internal Service Fund. This fund was established during the 2001 Legislative Session to reduce General Fund in the Department. Because the divisions were required to absorb this cost, the Department billed only actual costs and did not include the cost of compensated absences for the one staff member with accrued sick and annual leave. If turnover had occurred, the position would have remained open to cover the cost of the payout. The rates for the FY04/05 biennium will recover a portion of the compensated absence liability, and the remainder will be built into the rates to be presented to the 2005 Legislature. This recommendation will be proposed to the 2005 Legislative Session.

Statewide Fueling Program. Historically the legislature dual funded this program with general fund and an internal service fund to encourage use of the program. The program now has enough volume to fund costs solely through an internal service fund. Therefore the last legislature budgeted this program 100% as an internal service fund. Starting July 1, 2003, the proportionate amount of the one employee's salary who administers this program will be recovered by the fueling rate. This recommendation is implemented.

Procurement Card. We will lower the card fee to reduce the fund balance in this program. This recommendation will be implemented in Fiscal Year 2004.

Central Stores Program. We implemented two rate reductions in the fall of 2002 and this program is in compliance. This recommendation is implemented.

RECOMMENDATION #2: WE RECOMMEND THE DEPARTMENT MAINTAIN STATE EMPLOYEE GROUP BENEFIT PLANS ON AN ACTUARIALLY SOUND BASIS AND ENSURE RESERVES ARE SUFFICIENT TO COMPLY WITH SECTION 2-18-812, MCA.

Response: We concur. In order to restore the state employee group benefits plans to an actuarially sound basis, the department is taking the following steps:

In the short term, the department is implementing mid-year plan changes effective July 1, 2003 to contain costs. Changes are to add a $100 deductible for retail prescription drugs, a $50 deductible for certain dental services and a $1,000 annual cap on dental services. This will save about $1.3 million in the 2003 plan year.

The department requested the legislature approve an increase in the state share by $44 per month effective July 2003 instead of January 2004. This action was included in HB13, the state employee pay bill. This will increase plan income by about $3.1 million for the 2003 plan year.

Future changes such as benefits adjustments or premium increases will be determined based on the trends experienced and overall performance of the plans. Changes will be made with the intent to bring the plan into compliance (with the required reserves) by the end of the 2005 plan year.

We have provided to the Legislative Auditors Office a separate document containing additional background and details regarding the operation of the plan and the approach the department proposes to implement to restore and maintain the actuarial soundness of the state employee group benefits plans.

RECOMMENDATION #3: WE RECOMMEND THE DEPARTMENT:

A. ENSURE FEES CHARGED ARE COMMENSURATE WITH COSTS AS REQUIRED BY SECTION 17-8-101, MCA.
B. ESTABLISH A SELF-INSURANCE AND A DEDUCTIBLE RESERVE FUND AS ALLOWED BY SECTION 2-9-202, MCA.

Response: We concur. We will submit a budget request for the 2007 biennium to OBPP and the Legislature that funds the RMTD on an actuarially sound basis as recommended by this report. Should these funding efforts fail, we will work with the Legislature to change statute to avoid the significant fiscal impact that would result from implementation of the recommendation.

If the Risk Management & Tort Defense Division adopts the Legislative Audit Division's proposal, it is estimated that rates for this internal service fund will increase from $14.7 million to $49,587,734 (over the '07 Biennium') as shown below:

Estimated Claims Liability for all Prior Year's Losses as of 06/30/05	$29,848,481
Prospective Claims Liability for FY2006 (Actuarial Report 05/30/03)	$10,130,237
Prospective Claims Liability for FY2007 (Actuarial Report 05/30/03)	$10,805,580
Total Estimated Claims Liability for the '07 biennium'	$50,784,298
Less: Projected Cash Balance (State Self-Insurance Fund) 6/30/05	$ 1, 196,564
Estimated Unfunded Claims Liability (End of '07 biennium)	$49,587,734

The Risk Management & Tort Defense Division notes that during the '05 biennial' legislative session, internal service fund increases of $6,710,148 (or 83%) for FY2004 and $7,392,900 (or 92%) for FY2005 were approved by the legislature. These increases are incremental from FY2002 base and capture all projected costs for the '05 biennium' on a 'cash basis' including operational expenditures, commercial excess insurance, property/casualty claims, and tort litigation.

The Risk Management & Tort Defense Division also notes that rates submitted by the division and approved by the legislature for the '05 biennium' were based upon the previous three year's losses (two of the three years were historical worst loss years) and leave the state self-insurance fund with a projected ending balance of $1,196,564 to cover unexpected expenses.

A change in the historical current method of funding from a 'cash basis' to fully funding all prospective loss costs on an actuarial basis as suggested by the Legislative Audit Division will result in the above very significant internal service fund rate increases.

Options to Consider

(1) Amend the law to allow RMTD to continue to fund on a 'cash basis' as the division has done historically.
(2) Partially fund total estimated claims liability as other states have done. This would also require a statutory change.

(3) Partially fund prior year's losses (i.e. losses that occurred prior to 07/01/05) and fully fund prospective losses (i.e. FY06 and FY07) as determined by actuarial reports at 07/01/05.

RECOMMENDATION #4: WE RECOMMEND THE DEPARTMENT RECONCILE BALANCES ON THE STATE'S ACCOUNTING RECORDS TO THE BANK RECORDS.

Response: We concur. All outstanding reconciling items that agencies have failed to respond to have been moved to a clearing account in that agency, and the Accounting Bureau will follow up at year end to make sure the account is cleared. The Department's cash reconciliation from July 1999 through April 2003 shows the accounting system has approximately $360,000 more in cash than the bank records. In conjunction with MSU-Bozeman, we have determined that a large part of that cash is incorrectly recorded in MSU-Bozeman's records and are working with them to identify that amount. We will have the reconciliation completed by July 31, 2003.

With the implementation of the new cash policy and the electronic bank statement put in place this fiscal year that allows the Treasury Unit to reconcile the majority of wires received by state agencies, we believe cash reconciliation will not be an issue in upcoming years.

RECOMMENDATION #5: WE RECOMMEND THE DEPARTMENT ENSURE EFFECTIVE INTERNAL CONTROLS EXIST TO ENABLE PERSONNEL TO CARRY OUT THEIR RESPONSIBILITIES.

Response: We concur. Treasury Unit personnel have developed a line of communication with Department of Transportation personnel, which allows both agencies to receive the information necessary to perform their jobs. This recommendation has been implemented.

RECOMMENDATION #6: WE RECOMMEND THE DEPARTMENT CLARIFY THE FEBRUARY 6, 2003, POLICY MEMO FOR AGENCIES.

Response: We concur. The first page of the cash policy implemented on March 2003 is unclear as to what is expected of interface agencies. That language will be clarified and the management memo redistributed by July 1, 2003.

RECOMMENDATION #7: WE RECOMMEND THE DEPARTMENT COMPLY WITH:

A. SECTION 2-18-308, MCA, RELATED TO EMPLOYEE MILEAGE REIMBURSEMENT;

B. SECTION 32-5-308, MCA, REQUIRING CERTAIN INFORMATION ON CONSUMER LOAN ANNUAL REPORTS; AND
C. ADMINISTRATIVE RULES THAT SET GUIDELINES FOR SECURITY DEPOSITS.

Response:

A. We concur. At the conclusion of the August 2002 Special Session, the Department discussed legislative intent of the modified mileage reimbursement statute with Legislative Fiscal Division Staff, OBPP staff, staff from Department of Transportation who were involved in hearings related to this statute change and reviewed the fiscal note. The Department then applied the 52 percent to the standard reimbursement rate as defined by State travel policy, which we believe was legislative intent. The Department will seek to clarify the language on mileage reimbursement during the 2005 Legislative Session.
B. We concur. The Consumer Loan Act was passed in 1959, and over the years the methods of operation have changed while the Act hasn't always kept pace. Currently, many of the State's licensees are branches of regional or national firms rather than independent, stand-alone businesses. Because of this, many licensed offices do not have complete balance sheets – they have assets and liabilities, but their parent companies do not allocate any net worth components to the branches. Thus, not all of the annual report components required by the Act are available, and that's a trend we expect to continue. We plan to propose an amendment to this statute during the 2005 Legislative Session to bring reporting requirements into conformance with current operating practices.
C. We concur. We will ensure the administrative rules will be followed. The recommendation will be implemented immediately.

RECOMMENDATION #8: WE RECOMMEND THE DEPARTMENT ENSURE THE STATE'S ACCOUNTING RECORDS ACCURATELY REFLECT ACTIVITY OF THE STATE BY FISCAL YEAR END AS REQUIRED BY LAW.

Response: We concur. This issue deals with how prior year depreciation is recorded in SABHRS. A management memo on depreciation of capital assets through the Asset Management module will be distributed to all agencies in June 2003. This management memo will instruct agencies on how to appropriately record capital assets in the Asset Management module so that depreciation is recorded in the correct year.

Prepaid expenses are not normally used by the Department to make payments. The original payment to the US Dept of Health and Human Services used a valid appropriation. However, the federal government required the state to use two warrants since the payment included two fiscal years. The SABHRS system combined the payments into one warrant, and the process takes two days to cancel the warrant and return the appropriation authority to the agency. The payment took place within two days of fiscal year end 2002, so the only way to get the payment reissued immediately as requested by the federal government was to use a prepaid expense. The prepaid expense was immediately reversed after fiscal year end 2002. The Department will not use prepaid expenses in the future to make payments. This recommendation is implemented.

The Department will review balance sheet accounts at the end of fiscal year 2003 to ensure all balances are reconciled. The Department will also closely review all capital leases to ensure the correct amount is capitalized at fiscal year end 2003. This recommendation will be implemented by July 31, 2003.

We appreciate the opportunity to work with your staff on these issues.

Sincerely,

Scott Darkenwald

SCOTT DARKENWALD
Director